Teck Resources Ltd.: Next Stop $40?

Description

Teck Resources Ltd. (TSX:TCK.B)(NYSE:TCK) just hit $25 per share for the first time in 2016, and investors are wondering if the rally can continue.

Let's take a look at the current situation to see if Teck should be in your portfolio.

Zinc, copper, and metallurgical coal

Teck is Canada's largest diversified mining company with large zinc, copper, and coal operations.

The commodity rout over the past five years hammered all three divisions and sent Teck's stock tumbling from $60 per share in early 2011 to $4 per share in January of this year.

With $9 billion in debt and a weak outlook for coal and copper, Teck's days seemed numbered.

Then things began to turn around.

Zinc started the rally as investors realized significant production cuts were driving the market back into balance. The metal has surged 50% this year, and analysts think more gains could be on the way as demand rises.

Copper finally bottomed out and is slowly staging a recovery. The metal has traded in a range for most of this year, but pundits say the long-term outlook is positive.

Coal is this year's biggest surprise. In fact, it wasn't supposed to do well at all in 2016, but improved demand in India, supply issues in Australia, and regulatory changes in China have sent the spot price sky high in recent months.

What's the scoop?

China's decision to restrict the number of hours coal miners can work has had the largest impact onthe market. The reduction in output has been significant enough to drive metallurgical coal spot pricesup more than 100% to four-year highs above US$200 per tonne.

Most producers deliver coal on quarterly contract prices, so the surge is not going to have a large impact on Q3 results, but the settlement prices for the coming quarters might move significantly higher.

How high?

Bloomberg just reported a possible Q4 settlement price of US$200 per tonne being paid by steelmaker Nippon Steel to American producer Peabody Energy.

Teck's coal settlement price for Q3 was slightly above US$90 per tonne, and analysts have speculated new agreements would be around US$120-150 per tonne for the coming quarter.

Oil factor

Teck doesn't produce oil, but the company has a 20% stake in the Fort Hills oil sand development. When oil dropped below US$30 per barrel in January, investors figured the Fort Hills investment would be a write-off and dumped the stock.

With WTI oil back at US$50, the market is feeling better about Fort Hills, which is scheduled to begin production in late 2017.

Balance sheet

Teck's $9 billion debt load was another reason for the extended slide in the stock price, as investors started to worry about a potential cash crunch. The improvement in the company's market capitalization and the successful replacement of notes that were coming due in the next three years have reduced the debt concerns.

Could Teck hit $40?

The last time Teck rallied from $4 per share, it hit $60 within two years. Investors shouldn't assume a repeat is in the cards, but positive momentum remains in place.

If Teck manages to get US$200 per tonne for its coal in Q4 and the market believes the price gains are here to stay, this stock should continue to move higher on the back of earnings upgrades.

CATEGORY

1. Investing
2. Metals and Mining Stocks

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